

Message Text

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ORIGIN EB-08

INFO OCT-01 EUR-12 ISO-00 AGRE-00 TRSE-00 COME-00
INT-05 FEA-01 CIAE-00 INR-07 NSAE-00 L-03 PA-01
PRS-01 USIA-06 /045 R

DRAFTED BY EB/ISM:MZINOMAN:GMR
APPROVED BY AB/ICD:EAWENDT
EBISM:ACHEWITT
AGR:REINSAL
EUR/CAN:BLAKEMORE
TREA:HGALE
-----261852Z 127798 /50
R 260243Z MAR 77
FM SECSTATE WASHDC
TO AMEMBASSY OTTAWA
INFO AMCONSUL WINNIPEG

C O N F I D E N T I A L STATE 067414

E.O. 11652: GDS

TAGS: -MIN, CA

SUBJECT:POTASH SUPPLY ASSURANCES

REF: A) STATE 226722
B) OTTAWA 4419
C) WINNIPEG 0087

1. REGRET LONG DELAY IN REPLYING TO REF ,. QUESTIONS
POSED IN REF B, PARA 5 ARE CLEARLY CENTRAL TO ANY ASSESS-
MENT OF DANGER TO US AGRICULTURAL INTERESTS INHERENT IN
SASKATCHEWAN POTASH SITUATION. WE HAVE COORDINATED
CLOSELY WITH BUMINES AND AGR/ERS IN STUDYING YOUR QUESTIONS
AND FORMULATING FOLLOWING REPLY. YOU WILL NOTE, HOWEVER,
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THAT WE ARE NOT ABLE TO PROVIDE PRECISE PRICE AND
ELASTICITY INFORMATION REQUESTED BECAUSE OF DIFFICULTY IN
OBTAINING DATA ON PRODUCTION COSTS AND OTHER FACTORS.

2. REF B-PARA 5-QUESTION A:

SHOULD GOS SUCCEED IN ACQUIRING ITS GOAL OF 50 PERCENT

OWNERSHIP OF PROVINCE'S POTASH PRODUCTION, THERE IS LITTLE QUESTION THAT IT WOULD HAVE CAPABILITY TO RAISE PRICE,

ABOVE CURRENT LEVELS AND HAVE A SUBSTANTIAL IMPACT ON US

FARMER COSTS IN SHORT AND MEDIUM TERM. SHOULD GOS DECIDE TO UTILIZE THIS MARKET POWER, HOWEVER, IT WOULD RUN RISK OF STIMULATING ACCELERATED INVESTMENT IN ALTERNATIVE SOURCES IN US AND OTHER PARTS OF CANADA AND CERTAINLY PROD CONSUMERS TO CAST AROUND FOR OFF-SHORE SOURCES OF SUPPLY.

3. BECAUSE OF EXISTENCE OF SOVIET AND GERMAN SUPPLIER;, HOWEVER, GOS POWER IN WORLD MARKET IS MUCH MORE LIMITED THAN IN NORTH AMERICA. GOS HAS BEEN SUCCESSFUL IN DEVELOPING MARKETS FOR POTASH IN JAPAN AND BRAZIL, BUT HAS HAD LITTLE SUCCESS COMPETING WITH EUROPEAN SUPPLIERS IN WESTERN EUROPEAN MARKET AND THE U.S. REMAINS THE MAIN OUTLET FOR THEIR PRODUCT TAKING ABOUT 60 PERCENT OF ANNUAL PRODUCTION. TRANSPORTATION COSTS SHOULD CONTINUE TO OBSTRUCT CANADIAN EFFORTS TO CRACK EUROPEAN MARKET. POSSIBLE DANGER TO WORLD MARKET, OF COURSE, WOULD INVOLVE SOME FORM OF COLLUSION, EITHER TACIT OR OTHERWISE, BETWEEN GOS AND EUROPEAN SUPPLIERS.

4. REF B-PARA 5-QUESTION 0:

PRECISE PRICE LEVELS AT WHICH ALTERNATIVE NORTH AMERICAN SOURCES MIGHT ENTER THE MARKET CANNOT BE DETERMINED AT THIS TIME, SINCE THESE SOURCES ARE STILL BEING CONFIDENTIAL

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EXPLORED AND COSTS OF BRINGING PRODUCTION ONSTREAM ARE OPEN TO MAJOR UNCERTAINTIES. TWO US COMPANIES HAVE JUST COMPLETED EXPLORATIONS IN NEW BRUNSWICK AND INTEND TO CONTINUE ON TO THE NEXT STAGE OF DEVELOPING A PRODUCTION CAPABILITY. EXPLORATIONS OF DEPOSITS IN MONTANA AND NORTH DAKOTA ARE CONTINUING AND, ACCORDING TO BUMINES, THE COMPANIES INVOLVED CURRENTLY APPEAR BULLISH ABOUT PROSPECTS. IN ANY EVENT, PRODUCTION FROM THESE SOURCES IS AT LEAST FIVE YEARS OR MORE IN THE FUTURE, EVEN IF IT IS DETERMINED TO BE ECONOMICALLY FEASIBLE TODAY.

5. POSSIBILITY OF SOVIETS AS ALTERNATIVE SOURCE IS ALSO DIFFICULT TO MEASURE PRECISELY. NO EFFECTIVE COSTING SYSTEM IS AVAILABLE TO DETERMINE THE COMPETITIVE COST OF RUSSIAN POTASH. SOVIET PRICES TO WESTERN EUROPE, EVEN IF THEY COULD BE DETERMINED, ARE ADMINISTERED PRICE, AND NO GUARANTEE EXISTS THAT A SIMILAR STRUCTURE OF PRICES WOULD EXIST FOR SALES TO THE US.

6. IT IS ESTIMATED THAT BY 1980, SOVIETS AND EASTERN EUROPE WILL HAVE ;6 MILLION ST EXPORT SURPLUS (TVA ESTIMATE). SOVIETS HAVE BEEN DISCUSSING SWAP DEALS WITH US COMPANIES, INVOLVING USSR POTASH FOR US SUPERPHOSPHATES, AND THE SOVIETS HAVE HINTED THAT THEY MIGHT BE WILLING TO PROVIDE FREIGHT SUBSIDIES IN ORDER TO SELL POTASH IN US

MARKET. THESE INDICATIONS SUGGEST AT LEAST SOME SOVIET INTEREST IN MARKETING IN US AND SHOULD GOS PRICE OF POTASH RISE SUFFICIENTLY, US CONSUMERS MIGHT SOMEDAY FIND USSR AN EAGER AND VIABLE SOURCE OF SUPPLY.

7. REF B-PARA 5-QUESTION C:

IN THE SHORT RUN, AN EXTREME PRICE INCREASE (20 TO 25 PERCENT) WOULD RESULT IN SOME DECREASE IN QUANTITY OF POTASH USED, AS THE SOILS CAN WITHSTAND ONE TO TWO YEARS OF CONFIDENTIAL

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REDUCED APPLICATION WITH ONLY MINOR REDUCTION IN CROP OUTPUT. POTASH IS AN ESSENTIAL PLANT NUTRIENT FOR WHICH NO ALTERNATIVE EXISTS, SO THAT IN THE LONG RUN PRICE ELASTICITY WOULD BE QUITE LOW. HOWEVER, SOME REDUCED LEVEL OF USE MIGHT OCCUR IN THE LONG RUN, IF POTASH PRICES INCREASED RELATIVE TO THE PRICES OF THE COMMODITIES PRODUCED.

8. IN SUM, WE AGREE THAT GOS MAY ACQUIRE SUFFICIENT MARKET POWER TO BE ABLE TO RAISE POTASH PRICES WELL OVER THEIR FREE MARKET LEVEL AND THAT THIS WOULD HAVE A SERIOUS EFFECT ON US AGRICULTURE. HOWEVER, WE ALSO BELIEVE THAT GOS UNDERSTANDS THAT FOLLOWING SUCH A POLICY COULD PROVE SHORT-SIGHTED AND EVENTUALLY RISK LOSS OF A SUBSTANTIAL PORTION OF ITS AMERICAN MARKET.

9. WE APPRECIATE THE VALUE OF LONG-TERM SUPPLY AGREEMENTS BETWEEN GOS AND INDIVIDUAL US BUYERS AND WOULD CERTAINLY

NOT OPPOSE THEM IF APPROACHED BY US COMPANIES. HOWEVER, WE DO QUESTION WHETHER THE USG SHOULD BECOME ACTIVELY INVOLVED IN ENCOURAGING US FIRMS TO CONCLUDE THESE AGREEMENTS. WE WOULD DEFINITELY NOT WISH TO APPEAR AS AGENTS (EVEN INADVERTENTLY) OF THE GOS IN URGING THESE ARRANGEMENTS. SHOULD THE AGREEMENTS SUBSEQUENTLY SOUR, US COMPANIES MIGHT HOLD THE USG LIABLE FOR LOSSES INCURRED. IDEALLY, ARRANGEMENTS SHOULD BE CONCLUDED PURELY ON BASIS OF COMMERCIAL CONSIDERATIONS AND THE GOS, WHICH APPEARS ANXIOUS FOR THESE AGREEMENTS IN ORDER TO ASSURE A MARKET FOR ITS OUTPUT, SHOULD HAVE TO OFFER TERMS ATTRACTIVE ENOUGH TO ATTRACT US CONSUMERS.

10. WE NOTE THAT LATEST GOS PURCHASE OF POTASH PRODUCTION
FACILITIES, REPORTED IN REF C, HAS A FIVE YEAR SUPPLY
GUARANTEE AGREEMENT WITH A US COMPANY ASSOCIATED WITH IT.
WE WOULD BE INTERESTED IN WHETHER A SIMILAR ARRANGEMENT
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WAS INVOLVED IN THE DUVAL PURCHASE.
CHRISTOPHER

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: SUPPLIES, POTASSIUM, MINING INDUSTRY, DIPLOMATIC DISCUSSIONS
Control Number: n/a
Copy: SINGLE
Sent Date: 26-Mar-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977STATE067414
Document Source: CORE
Document Unique ID: 00
Drafter: MZINOMAN:GMR
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D770105-0097
Format: TEL
From: STATE
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770319/aaaaapsg.tel
Line Count: 183
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
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Office: ORIGIN EB
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: 77 STATE 226722
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 21-Dec-2004 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 2985562
Secure: OPEN
Status: NATIVE
Subject: POTASH SUPPLY ASSURANCES
TAGS: EMIN, CA, US
To: OTTAWA
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/5cfd39b1-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009